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SUBJECT: AUSTRALIAN RESERVE BANK HOLDS RATES AMID MIXED ECONOMIC
NEWS

¶1. (U) SUMMARY: The Reserve Bank of Australia decided to leave interest rates unchanged at 3.25%, despite mixed economic news and increased reports of job losses. The RBA indicated that monetary and fiscal policy changes have been significant and need to work through the Australian economy before further changes are considered. END SUMMARY.

¶2. (U) The RBA decided March 3 to leave the cash rate unchanged at 3.25 per cent. In a statement released by Governor Glenn Stevens, the RBA noted the world economy remains "very weak", but emphasized that demand in Australia has not weakened as much as in other countries. Stevens said that the Australian economy has not experienced the sort of large contraction seen elsewhere, the Australian financial system remains strong and monetary policy (400 basis point cut in the rate since September) is delivering large reductions in interest rates to end borrowers. The RBA concluded that very low market, mortgage rates, and business loan rates plus the GOA's fiscal stimulus packages would significantly support demand, so a further interest rate cut was not necessary.

¶3. (U) The decision to leave the rate unchanged was a mild surprise. A string of mixed economic news over recent days had created an expectation of a cut. On the good side of the ledger was a better-than-expected performance in the retail sector, with sales up 0.2 per cent over January in seasonally adjusted terms. The Housing Industry Association on March 3 reported that new home sales jumped 8% in January from the previous month - boosted by the increase in the first-time buyer assistance from the first stimulus package.

¶4. (U) On the negative side, job losses continue to mount. Last week Pacific Brands, Australia's largest clothing manufacturer, announced it would shift its domestic manufacturing to China at a cost of 1850 jobs. Anglo Coal announced it will cut 650 mining jobs in Queensland and New South Wales, while car parts maker Robert Bosch is making 170 workers redundant. The Australian Bureau of Statistics announced March 2 large drops in company profits (6.5% for the December quarter - only the mining sector showing an increase) and in inventory (1.9%), with experts uncertain whether that was the result of the stimulus-fueled better-than-expected Christmas season or due to firms slashing orders.

¶5. (U) On March 4 the December quarter national accounts will be released. Some fear it could be negative, and that growth for the September quarter may be revised downward from 0.1% possibly to negative territory - meaning Australia would have entered recession in 2008. However, the RBA has access to the national account data and presumably judged that the news was not sufficiently negative to cut justify another cut in interest rates. A bump in inflation in January and February indicated by the TD-Melbourne Institute - and

rising gasoline prices - probably also contributed to the RBA's non-move. There has been positive news on Australia's external accounts, with a current account deficit of \$A6.5 billion in the December quarter. The deficit has narrowed by nearly A\$3 billion, or about a third, from the quarter before. The surplus on goods and services increased by A\$2.7 billion to A\$4.1 billion in the December quarter. Australia's net foreign debt is still of concern at \$A678.3 billion. However, bad news is likely in the future and now seven out of Australia's ten top trading partners are in recession.

15. (SBU) COMMENT: The Reserve Bank's decision to leave monetary policy unchanged suggests that it has confidence in the impact of the GOA's fiscal stimulus policies and the significant lowering of interest rates that has also occurred. A factor not mentioned by the RBA is that Australia needs to continue to attract international portfolio and direct investment to finance its current account deficit and large foreign debt. Maintaining higher interest rates is likely to support such flows. END COMMENT.

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